

## **COMMODITY FUTURES TRADING COMMISSION**

### **Performance of Notice Registration Processing Functions by National Futures Association With Respect to Certain Securities Brokers and Dealers**

**AGENCY:** Commodity Futures Trading Commission.

**ACTION:** Notice and order.

**SUMMARY:** The Commodity Futures Trading Commission (“Commission”) is authorizing the National Futures Association (“NFA”), effective [Insert date 30 days after date of publication in the FEDERAL REGISTER], to process notice registration filings as a futures commission merchant (“FCM”) or introducing broker (“IB”) in the case of a securities broker or dealer (“BD”) registered with the Securities and Exchange Commission (“SEC”) that, among other things, limits its involvement with commodity futures contracts to security futures products. In addition, the Commission also is authorizing NFA (1) to terminate any such registration in the event the criteria upon which it was based are no longer satisfied, (2) to maintain, on behalf of the Commission, records regarding BDs notice-registered as an FCM or IB, and (3) to serve as the official custodian of those Commission records. This Order does not, however, authorize NFA to grant conditional registrations to BDs notice-registered as an FCM or IB or, except as stated above, to deny, revoke, suspend or take any other adverse actions with respect to such registrations. This Order also does not authorize NFA to accept or act upon requests for exemption, “no-action” or interpretative letters with respect to applicable registration requirements.

**EFFECTIVE DATE:** [Insert date 30 days after date of publication in the FEDERAL REGISTER].

**FOR FURTHER INFORMATION CONTACT:** Barbara S. Gold, Assistant Chief Counsel, or Lawrence B. Patent, Associate Chief Counsel, Division of Trading and Markets, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21<sup>st</sup> Street NW., Washington, DC 20581, (202) 418-5450, electronic mail: bgold@cftc.gov, or lpatent@cftc.gov.

**SUPPLEMENTARY INFORMATION:**

**I. Authority and Background**

In a separate notice published elsewhere today in the **Federal Register**, the Commission is amending its rules to implement the Congressional mandate in Section 252(b) of the Commodity Futures Modernization Act of 2000 (“CFMA”)<sup>1</sup> requiring notice registration as an FCM or IB of certain SEC-registered BDs if:

(A) the broker or dealer limits its solicitation of orders, acceptance of orders, or execution of orders, or placing of orders on behalf of others involving any contracts of sale of any commodity for future delivery, on or subject to the rules of any contract market or registered derivatives transaction execution facility to security futures products;

(B) the broker or dealer files written notice with the Commission in such form as the Commission, by rule, may prescribe containing such information as the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors;

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<sup>1</sup> Pub. L. No. 106-554, 114 Stat. 2763. The provision in question will be codified at Section 4f(a)(2) of the Commodity Exchange Act (“CEA”), 7 U.S.C. 6f(a)(2).

Because the CFMA speaks in terms of a “broker or dealer,” the term “BD as used in this release applies equally to a broker, a dealer or a person registered as both a broker and a dealer.

(C) the registration of the broker or dealer is not suspended pursuant to an order of the Securities and Exchange Commission; and

(D) the broker or dealer is a member of a national securities association registered pursuant to section 15A(a) of the Securities Exchange Act of 1934.

Specifically, the Commission is amending Rule 3.10 by adding paragraph (a)(3) to provide for such notice registration.<sup>2</sup>

As proposed and as adopted, Rule 3.10(a)(3) provides that this notice registration may be made “by following such procedures . . . as may be specified” by NFA. As the Commission explained in proposing paragraph (a)(3), this is consistent with the Commission’s previous delegations of registration authority to NFA under Rule 3.2 and through various Commission orders.<sup>3</sup> The Commission further explained that this also is consistent with Section 125 of the CFMA, which requires the Commission to report to Congress later this year on a study of the CEA and the Commission’s rules, regulations and orders governing the conduct of persons required to be registered under the CEA. In this regard, the Commission noted that one area that the study must identify is “the regulatory

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<sup>2</sup> Commission rules referred to herein generally are found in 17 CFR Ch. I (2001).

<sup>3</sup> See, e.g., 48 FR 15940 (April 13, 1983); 48 FR 35158 (August 3, 1983). Section 8a(10) of the Act, 7 U.S.C. 12a(10), provides that the Commission may authorize any person to perform any portion of the registration functions under the CEA, notwithstanding any other provision of law, in accordance with rules adopted by such person and submitted to the Commission for approval, or, if applicable, for review pursuant to section 17(j) of the CEA, 7 U.S.C. 21(j), and subject to the provisions of the CEA applicable to registrations granted by the Commission. See also section 17(o) of the CEA, 7 U.S.C. 21(o).

functions the Commission currently performs that can be delegated to a registered futures association.”<sup>4</sup>

NFA Registration Rule 204, like Commission Rule 3.10, concerns the registration of persons as FCMs and IBs. On May 17, 2001, NFA’s Board of Directors approved a proposed amendment to Rule 204 so as to conform NFA’s rule to that proposed by the Commission for notice registration of certain BDs as an FCM or IB.<sup>5</sup>

Upon consideration, the Commission has determined to authorize NFA, effective [Insert date 30 days after date of publication in the FEDERAL REGISTER], to perform notice registration functions as set forth in Rule 3.10 in accordance with the standards established by Section 4f(a)(2) of the CEA. The Commission is further authorizing NFA, under specified conditions, to terminate any such registration and to perform records custodian functions with respect to notice registration under Rule 3.10. Concurrently, the Commission is separately approving on this date NFA’s proposed amendment to its Registration Rule 204.<sup>6</sup>

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<sup>4</sup> See 66 FR 27476 at 27478 (May 17, 2001).

<sup>5</sup> NFA’s proposed amendments to Rule 204 also provide that notice registration under that rule “shall be terminated immediately if any of the conditions set for [such] registration are no longer satisfied.” Inasmuch as the Commission adopted as proposed the amendments to Rule 3.10, the Commission similarly approved as proposed NFA’s amendments to Rule 204.

<sup>6</sup> Notice registration will be made on Notice Form 7-R, which was included in the NFA notice registration submission that the Commission approved.

The Commission further notes that section 17(p)(1) of the CEA<sup>7</sup> requires that each registered futures association (such as NFA) “establish training standards and proficiency testing for \* \* \* all persons for which it has registration responsibilities.” While this provision of the CEA would appear to require NFA to establish testing requirements for securities BD applicants for notice registration as an FCM or IB, the Commission believes that it is not the intent of Congress to require testing of these applicants. This is because Section 252(c) of the CFMA provides that a BD notice-registered as an FCM or IB “shall not be required to become a member of any futures association registered under section 17.”<sup>8</sup> The Commission also notes that testing requirements are generally intended to apply to associated persons, and associated persons of BDs that notice register as an FCM or IB are specifically exempted from registration under Section 4k(5) of the Act, as added by Section 252(d) of the CFMA. In light of the foregoing, the Commission has determined to adopt a “no-action” position with respect to the establishment by NFA of a proficiency testing

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<sup>7</sup> 7 U.S.C. 21(p)(1).

<sup>8</sup> This provision has been codified at section 4f(a)(4)(C) of the CEA.

In proposing amendments to Rule 3.10 the Commission explained that:

[a]lthough the Commission cannot require NFA to perform registration functions for persons that are not NFA members, the Commission may authorize NFA to perform any registration function. Commission staff have discussed this matter with NFA, and NFA has agreed to undertake the function of processing notice registrations for BDs as discussed herein. If the Commission adopts these amendments to Rule 3.10, it expects to issue an order authorizing NFA to perform this function. 66 FR 27476 at 27478.

requirement for BDs who notice register as FCMs or IBs. Accordingly, the Commission will not institute any enforcement action under section 17(p)(1) of the CEA against NFA based solely upon NFA's failure to establish training standards and proficiency testing for these BDs even though NFA is being authorized to perform certain registration functions with respect to these BDs.<sup>9</sup>

Section 17(o)(2) of the CEA provides that the Commission may authorize NFA, in performing Commission registration functions, to deny, condition, suspend, restrict or revoke any registration, subject to Commission review.<sup>10</sup> As stated above, NFA Registration Rule 204, which the Commission has today approved, provides that BD notice registration as an FCM or IB "shall be terminated immediately if the other conditions set for [such] registration are no longer satisfied." The Commission is not at this time, however, authorizing NFA to take any other adverse registration actions with respect to the BD notice registration applications that it processes pursuant to this Order. This is consistent with Section 252 of the CFMA.

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<sup>9</sup> This treatment of NFA concerning testing requirements for these BDs is similar to the Commission's position regarding testing requirements for floor traders. See 58 FR 19657 at 19658 (April 15, 1993). The Commission further notes, however, that the futures and securities industry self-regulatory organizations, including NFA, are developing enhancements to existing proficiency examinations, as well as training modules for existing registrants, so that industry professionals will be aware of their responsibilities to the public concerning security futures products.

<sup>10</sup> 7 U.S.C. 21(o)(2).

By prior orders, the Commission has authorized NFA to maintain various other Commission registration records and certified NFA as the official custodian of such records for this agency.<sup>11</sup> The Commission has now determined, in accordance with its authority under Section 8a(10) of the CEA,<sup>12</sup> to authorize NFA to maintain and serve as official custodian of the Commission's registration records with respect to BDs notice-registered as an FCM or IB.

In maintaining the Commission's registration records pursuant to this Order, NFA shall be subject to all other requirements and obligations imposed upon it by the Commission in existing or future Orders or regulations.<sup>13</sup> In this regard, NFA shall also implement such additional procedures (or modify existing procedures) as are necessary to ensure the security and integrity of the BD notice-registered records in NFA's custody as acceptable to the Commission; to facilitate prompt access to those records by the Commission and its staff, particularly as described in other Commission Orders or rules; to facilitate disclosure of public or nonpublic information in those records when permitted by Commission Orders or rules and to keep logs as required by the Commission concerning disclosure of nonpublic information; and otherwise to safeguard the confidentiality of the records.

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<sup>11</sup> See, e.g., 49 FR 39593 (October 9, 1984).

<sup>12</sup> 7 U.S.C. 12a(10).

<sup>13</sup> See, e.g., 49FR 35953 at 39595 – 97.

## **II. Conclusion and Order**

The Commission has determined, in accordance with the provisions of Section 8a(10) of the CEA, to authorize NFA, effective [Insert date 30 days after date of publication in the FEDERAL REGISTER], to perform the following registration functions:

- (1) To receive and maintain filings for notice registration under the Commodity Exchange Act as a futures commission merchant or introducing broker by those brokers and dealers registered with the Securities and Exchange Commission who meet the requirements of NFA Registration Rule 204;
- (2) To terminate the notice registration of a registered broker or dealer as a futures commission merchant or introducing broker where the broker or dealer no longer meets the requirements of NFA Registration Rule 204; and
- (3) To maintain records regarding brokers and dealers notice-registered as a futures commission merchant or introducing broker and to serve as the official custodian of those Commission records.

NFA shall perform these functions in accordance with the standards established by the CEA and the regulations promulgated thereunder.

These determinations are based upon the Congressional intent expressed in sections 8a(10) and 17(o) of the CEA and Section 125 of the CFMA. This Order does not, however, authorize NFA to accept or act upon requests for exemption from registration, to render “no-action” or interpretative letters with respect to applicable registration requirements, to grant conditional registrations, or, except as stated in item (2) above, to deny or take any other adverse action with respect to such registrations.



Nothing in this Order or in Sections 8a(10) or 17 of the CEA or in Section 125 of the CFMA shall affect the Commission's authority to review the performance by NFA of Commission registration functions.<sup>14</sup>

Issued in Washington, DC on \_\_\_\_\_, **2001**.

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**Jean A. Webb,**  
*Secretary of the Commission*

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<sup>14</sup> See also section 17(o)(3) of the CEA, 7 U.S.C. 21(o)(3).